

# SUMMARY ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Campbell Analyst: Marion Mann DeJong Bill Number: AB 735

Related Bills: See Prior Analysis Telephone: 845-6979 Amended Date: 03/26/2003

Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Taxpayer Privacy Bill of Rights Act/Expands Scope of Taxpayers' Rights Advocate to Include Taxpayers' Privacy Rights

DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended \_\_\_\_\_.

AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.

☒ AMENDMENTS DID NOT RESOLVE THE DEPARTMENT'S CONCERNS stated in the previous analysis of bill as introduced February 19, 2003.

☒ FURTHER AMENDMENTS NECESSARY.

DEPARTMENT POSITION CHANGED TO \_\_\_\_\_.

☒ REMAINDER OF PREVIOUS ANALYSIS OF BILL AS INTRODUCED February 19, 2003, STILL APPLIES.

OTHER - See comments below.

## SUMMARY

This bill would:

- Expand disclosure laws to prohibit Franchise Tax Board (FTB) officers or employees from releasing or threatening to release a taxpayer's personal or financial information to the general public.
- Specify conditions for FTB's disclosure of a taxpayer's financial or personal information in any court or administrative proceeding.
- Add a new cause of action allowing a taxpayer to file a lawsuit against FTB, its officers, or employees for damages resulting from unauthorized disclosure of personal or financial information.
- Expand the Taxpayers' Rights Advocate's (Advocate) authority to review and resolve taxpayer complaints and verify that appropriate disciplinary action is taken against any FTB officer or employee who violates a taxpayer's privacy rights.
- Require the Advocate to toll the accrual of any penalties and interest during a stay of action.

## SUMMARY OF AMENDMENTS

The March 26, 2003, amendments added provisions that:

- Specify conditions for FTB's disclosure of a taxpayer's financial or personal information.
- Added a new cause of action allowing a taxpayer to file a lawsuit for damages resulting from a specific unauthorized disclosure.

Board Position:

<input type="checkbox"/> S	<input type="checkbox"/> NA	<input type="checkbox"/> NP
<input type="checkbox"/> SA	<input type="checkbox"/> O	<input type="checkbox"/> NAR
<input type="checkbox"/> N	<input type="checkbox"/> OUA	<input checked="" type="checkbox"/> PENDING

Legislative Director  
Brian Putler

Date  
04/11/03

- Require the Advocate to toll the accrual of any penalties and interest during a stay of action.

The March 26, 2003, amendments did not resolve the concerns in the department's analysis of the bill as introduced. In addition, the amendments raise additional concerns. The "Purpose of the Bill," "Effective/Operative Date," "Legislative History," and "Other State's Information" discussions in the department's analysis of the bill as introduced still apply. The remainder of the previous analysis is replaced with the following. The Board position remains pending.

### **Summary of Suggested Amendments**

Amendments are needed to resolve the concerns raised in "Implementation Considerations." Department staff is available to assist the author with these amendments.

## **ANALYSIS**

### **FEDERAL/STATE LAW**

#### *Disclosure*

Existing federal and state laws prohibit the disclosure of any taxpayer information, except as specifically authorized by statute. Any FTB employee or member responsible for the unauthorized disclosure of federal or state tax information is subject to criminal prosecution, disciplinary action, and/or loss of employment. Improper disclosure of federal tax information is punishable as a felony and improper disclosure of state tax information is punishable as a misdemeanor.

The California Information Practices Act allows an individual to bring a cause of action for damages for unauthorized disclosure of personal information.

Department interpretation of the Revenue & Taxation Code (R&TC) provisions on the confidentiality of taxpayer information treats all information received, maintained, and generated as confidential unless it is specifically made public by statute. This includes federal, state, and local tax information, senior citizens' property tax assistance information, political reform audit information, personnel records, and criminal offender record information.

Current state law provides that a state officer or employer shall not engage in any employment, activity, or enterprise that is clearly inconsistent, incompatible, in conflict with, or inimical to his or her duties as a state officer or employee.

Written department policy lists activities that are inconsistent, incompatible, or in conflict with the duties of FTB employees. Incompatible activities include providing confidential information to persons to whom issuance of this information has not been authorized. Written department policy also provides rules of conduct for FTB employees. FTB officers and employees are prohibited from:

- disclosing confidential information in writing, electronically, or verbally to unauthorized individuals.
- indicating or implying that an examination of a tax return will be initiated as a reprisal against anyone.

It is department policy to investigate alleged violations of law, rules, regulations and/or internal policies relating to activities that are inconsistent, incompatible, or in conflict with the duties of FTB employees. Disciplinary action is taken under the Civil Service Act when appropriate. When there is evidence of significant criminal wrongdoing, the matter is referred to the appropriate prosecutor's office for consideration of criminal charges.

#### *Taxpayers' Rights Advocate*

The Taxpayers' Bill of Rights established the Taxpayers' Rights Advocate to coordinate the resolution of taxpayer complaints and problems, including any complaints regarding unsatisfactory treatment of taxpayers by FTB employees. The Advocate has authority to stay actions and toll the statute of limitations while resolving the taxpayer's concerns. Current law specifies that penalties and interest are not affected by the tolling, thus interest still accrues and penalties still apply.

Existing law allows a taxpayer to file a lawsuit against the State if an FTB officer or employee disregards FTB published procedures. The law permits the taxpayer to be awarded the amount of actual damages and reasonable litigation costs. A court may impose a penalty of up to \$10,000 against a taxpayer who files a frivolous case.

#### *Third Party Contacts*

Current state law authorizes the department to contact third parties to obtain information to determine and collect the taxpayer's tax liability and enforce the tax laws. Current law requires the department to notify the taxpayer that contact with a third party will be made. The purpose of the notification is to provide the taxpayer with an opportunity to volunteer whatever information is being requested. The notification is effective for 12 months. The taxpayer may request a list of third party contacts no later than 60 days after the end of the 12-month period.

#### *Judicial & Administrative Proceedings*

Applicable statutes, regulations, and case law govern the admissibility of evidence offered by the parties in judicial or administrative proceedings. Rules regarding the admissibility of evidence in judicial proceedings are codified in the California Evidence Code. Rules regarding the admissibility of evidence in proceedings before the State Board of Equalization (SBE) are found in regulations governing SBE proceedings. In general, evidence is admissible if it is relevant to the matters in dispute.

Generally, judicial and administrative proceedings are conducted in public. However, an adjudicative body has the authority to seal the records in a proceeding in certain circumstances. Under existing law the decision to seal otherwise public records is made by balancing the public right to access adjudicative proceedings, which carries great weight, against an individual's right to privacy. When granted, orders sealing documents are narrowly and specifically written. Orders to close proceedings or seal documents from the public are extraordinarily rare.

Current state law, known as the Bagley-Keene Open Meeting Act, generally requires deliberations of multi-member state bodies to be conducted in meetings open to the public. The SBE is a multi-member state body governed by the Bagley-Keene Open Meeting Act.

Under current law, taxpayers may appeal FTB's denial of a refund claim or denial of a protest to the SBE. These appeals necessarily involve tax return information that is prohibited from disclosure under general rules. Revenue and Taxation Code Section 19545 provides a specific exception allowing disclosure of taxpayer information in a judicial or administrative proceeding. Under current law, documents submitted as part of an appeal are public records, and, under open meetings rules, oral hearings on taxpayer appeals must be open to the public. The SBE then normally issues a written published opinion or unpublished decision that is also a public record.

Current law provides state agencies and employees general immunity from liability for activities relating to the assessment or collection of taxes, based on California's sovereign immunity. Specific exceptions to this immunity are contained in existing law, in California's torts claims statutes, and in the Taxpayer's Bill of Rights provision allowing suit and damage recovery where an FTB officer and employee disregards FTB published procedures.

### THIS BILL

This bill would establish the Taxpayer Privacy Bill of Rights. Specifically this bill would:

- Expand disclosure laws that prohibit the disclosure of return information to prohibit FTB officers or employees from releasing a taxpayer's personal or financial information to the general public, unless a compelling interest is shown by FTB and the courts authorize the disclosure. Unauthorized release of, or threat to release, this information for the purposes of coercing a settlement of the taxpayer's state tax liability would be grounds for termination or other disciplinary action, regardless of whether the release or threat to release the information was express or implied, intentional or negligent.
- Prohibit an FTB officer or employee from presenting a taxpayer's personal or financial information to a court or administrative agency in connection with any court or administrative proceeding unless all of the following are satisfied:
  1. The taxpayer's personal or financial information submitted by FTB is limited to that information that is essential to an issue or issues in the court or administrative proceeding.
  2. FTB has shown a compelling need for the submission of the information.
  3. The Information is filed under seal from the public.
- Add a new cause of action allowing a taxpayer who has sustained damages as a result of any unauthorized release of, or threat to release, the taxpayer's personal or financial information rather than return information, to pursue an action for damages against FTB, its officers, or employees.

This bill also would expand the Taxpayers' Rights Advocate's authority to review and resolve taxpayer complaints to specifically include complaints regarding the unauthorized release of taxpayers' personal and financial information to the general public by FTB officers or employees. The Advocate would verify that the board takes appropriate disciplinary action against any officer or employee who violates a taxpayer's privacy rights.

In addition, this bill would expand the Advocate's authority regarding staying actions to include the tolling of any penalties and interest.

## IMPLEMENTATION CONSIDERATIONS

- This bill does not define the phrase “a taxpayer’s personal or financial information” or the terms “general public,” “threat,” or “essential.” Clear definitions are necessary to ensure that the bill is implemented as the author intended and to prevent disputes between taxpayers and the department.
- This bill prohibits disclosure of certain information to the general public, unless authorized by the courts. This could be interpreted to prevent the department from contacting third parties without prior court approval. This could prevent the department from obtaining information necessary to determine the residency of a taxpayer. It could also hinder the department from obtaining information from a reliable source when a taxpayer refuses to provide requested information or when the department is verifying information provided by the taxpayer. If the department were required to seek authorization from a court before contacting any third party, the audit program would be significantly impacted. Audits would take longer and cost more to conduct. The bill would also impact the department’s criminal investigations program since it is unclear whether the department could subpoena third parties. Further, this bill could delay collection of taxes if the department is required to obtain permission from a court before issuing orders to withhold, issuing liens, or using any other collection method that involves third parties.
- This bill would require the entirety of a taxpayer’s personal or financial information to be sealed in a court or administrative proceeding. Sealing records of any kind is a legal and public policy decision—made on a case-by-case basis—and already reserved for a judge under existing law. Also, sealing information as provided by this bill conflicts with other provisions of the tax law that allow disclosure of a return or return information in a judicial or administrative proceeding pertaining to tax administration. It would also conflict with statutes that specifically provide for the disclosure of certain information in certain circumstances (e.g., parent locator service or legislative committee).
- This bill contradicts California’s existing public policies and laws that judicial and administrative proceedings be public. A taxpayer’s personal and financial information would be the subject of any tax proceeding. Under this bill, department staff could not advocate California’s position in any forum unless the process was closed to the general public, or the department has first obtained authorization to disclose this information from a court. This could increase costs such as cost to defend against a taxpayer’s appeal or suit for refund.
- This bill would restrict the information that FTB can present in a court or administrative proceeding to information essential to an issue or issues in that proceeding. This could result in disputes between taxpayers and the department regarding what information is essential, especially in residency or unitary cases where substantial detailed information involving personal, financial, and business operations of the taxpayers are obtained during the audit and that information is relevant to issues in dispute.

Further, by restricting personal or financial information submitted by FTB in a judicial or administrative proceeding to only that which is essential, this bill would establish a new rule of evidence for the admissibility of evidence, seemingly in addition to the relevance standard, in judicial and administrative proceedings where the FTB is a party.

- Although the taxpayer generally has the burden of proof, if a taxpayer does not provide enough information or discloses information that under this bill is confidential, it is unclear what right the department would have to refute the taxpayer's disclosure.
- This bill requires the Advocate to verify that the department takes appropriate disciplinary action against an employee who violates a taxpayer's rights. However, the bill does not provide the Advocate the authority to ensure that appropriate disciplinary action takes place. In addition, it does not specify what this verification should consist of or to whom it would be provided.
- The bill appears to allow only disciplinary actions and termination of employment. Currently, action taken against an FTB employee could include criminal charges, which could be taken under any circumstance regarding unauthorized disclosure.
- Because existing law authorizes release of necessary information in administrative proceedings and in court, it is imperative that if this legislation is enacted it specifically contain a prospective effective date and not impact existing judicial and administrative controversies. This would provide the department, the courts, and the SBE time to modify procedures and not disrupt those proceedings already in progress.

## **FISCAL IMPACT**

The department's costs to administer this bill cannot be determined until implementation concerns have been resolved. Audit activities that are dependent upon factual development, such as residency and unitary business audits, and collection activities, would likely be stopped while staff pursued court orders to obtain third party information. Department costs could increase for audit, legal, and collection activities as a result of this bill.

## **ECONOMIC IMPACT**

### Revenue Estimate

This bill would have a significant, negative impact on State income revenues easily exceeding \$500 million annually beginning January 1, 2004.

The department sets up over \$780 million annually in assessments from audits to individuals and corporations. Based on the percentage of assessments and the dollar amount of those assessments that could be impacted by this bill, it is projected that this bill would impact assessments in the range of \$350 million to \$450 million annually.

In addition, the department sends out over 61,000 individual levies monthly to banks, credit unions, savings and loans and employers to collect over \$400 million in cumulative taxes owed. If the department were required to obtain a court order for each one of these levies, these activities would be delayed and may be put at risk.

## **ARGUMENTS/POLICY CONCERNS**

- Requiring the records in a judicial or administrative proceeding to be sealed appears to conflict with the general policies of open meetings and freedom of information.

Generally, the public has a right to know how the government administers the tax laws. This bill could result in closed hearings before the Board of Equalization. These meetings are currently open to the public.

Further, since the facts of cases would be sealed, some tax cases would no longer set precedence for interpreting tax laws.

- Many laws protect taxpayers from inappropriate disclosure of information, yet give staff the authority to disclose appropriate information in administrative proceedings and in court. This law would put a burden on state employees personally to be sure that evidence is essential and a mistake in interpreting the law could result in personal liability.

## **LEGISLATIVE STAFF CONTACT**

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